

INDEPENDENT FACTORS LTD.

ANNUAL REPORT to SHAREHOLDERS

and

Consolidated Financial Statements for

The Year Ended 31 Dec. 1986

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INDEPENDENT FACTORS LTD.

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FACTORERS

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If You Need Money - See Your Banker.

IF YOU NEED EQUITY - SEE US - INDEPENDENT FACTORS LTD.

- WE PROVIDE THE WAY TO FINANCIAL PROSPERITY, BY:

- EQUITY FACTORING:
- EMPLOYEE EQUITY INCENTIVE PLANS
- FINANCIAL STABILITY PLANS
- BALANCE SHEET STRENGTHENING

Financially stable businesses create stable market systems.

PRESIDENT'S REPORT TO THE SHAREHOLDERS

EQUITY FACTORING: WHAT IT IS

When you borrow money to finance business expansion, you go to a Bank or other lenders of money.

Independent Factors Ltd. has gradually built up a business whereby it lends equity, not money, to finance businesses. Its equity base is its publicly traded shares. In these few paragraphs, I shall try to show how lending equity is developing, how it compares with early money lending, and why it is essential for financial stability in market systems.

The lending of money began in a number of ways. One early form of lending evolved from the sale of merchandise and goods on credit. From this developed factoring - the discounting for cash - of accounts receivable. From these beginnings, and the practices of the goldsmiths, banking and lending money - the nominal way to handle savings - has become a very simple, reliable, safe way for the average saver to hold savings.

There is as yet no equally safe, simple, reliable means to deposit and retract savings in equity. At least, that was so until INDEPENDENT FACTORS LTD.

What we have done is to create an equity deposit/lending business that is as safe, simple, and reliable for equity investment as the bank deposit system is for the money or nominal form of saving. That requires a clear understanding of the differences between money and equity.

We contend that there can easily be stable market systems free of the so-called business

cycle. Since the business cycle is caused by the cyclical variation of the liabilities /equity ratio, on the titles side of the balance sheet, and the (money and debt)/other assets ratio on the asset side, the stabilization of these will stabilize your business, and your business thus stabilized will contribute financial stability to its market area.

It follows that if all businesses are stable, the market is stable. This rather easily attained condition should not be difficult to maintain once we all understand something of the above ratios. We cannot accomplish our object of a stable market, however, until we have in fact built the sturdy financial structures that give us financial stability and that work in practice.

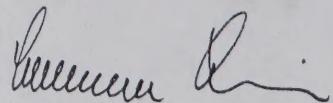
INDEPENDENT FACTORS LTD., now in operation for a decade - and operating as a publicly traded equity investment vehicle for the past six years plus, has shown that equity factoring - even in its rudimentary stages of development - can be and is a very profitable, and easily workable way to achieve financially stable markets.

INDEPENDENT FACTORS LTD. IS THE FIRST - NOTE IT WELL - :THE ORIGINAL EQUITY FACTORING COMPANY IN EXISTENCE.

That is why we say:

WHEN YOU NEED EQUITY, COME TO INDEPENDENT FACTORS.

I have saved the last word for our shareholders. Our efforts are directed toward giving you a safe reliable investment which is modestly liquid, gains well in the market, and has a stable value. If we succeed, equity factoring should be a major growth industry, and INDEPENDENT should be its leader.



INDEPENDENT FACTORS LTD.

CONSOLIDATED FINANCIAL STATEMENTS

31 DECEMBER 1986

DUNWOODY & COMPANY



Internationally
DUNWOODY ROBSON McGLADREY & PULLEN
Chartered Accountants
1408 Canyon Street, P.O. Box 1175, Creston, B.C.,
Canada V0B 1G0
Telephone: (604) 428-2248

AUDITORS' REPORT

TO THE SHAREHOLDERS

INDEPENDENT FACTORS LTD.

We have examined the consolidated balance sheet of Independent Factors Ltd. as at 31 December 1986 and the consolidated statements of income and retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Company as at 31 December 1986 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Dunwoody & Company

Creston, B.C.
27 February 1987

CHARTERED ACCOUNTANTS

INDEPENDENT FACTORS LTD.

CONSOLIDATED STATEMENT OF INCOME AND RETAINED EARNINGS
FOR THE YEAR ENDED 31 DECEMBER 1986

| | <u>1986</u> | <u>1985</u> |
|--|--------------------|--------------------------|
| SALES | \$5,222,848 | \$5,952,015 |
| COST OF SALES, SELLING AND ADMINISTRATIVE EXPENSES | <u>4,809,636</u> | <u>5,450,838</u> |
| OTHER INCOME | 413,212 105,342 | 501,177 <u>50,865</u> |
| | <u>518,554</u> | <u>552,042</u> |
| OTHER EXPENSES | | |
| Depreciation | 61,678 | 50,206 |
| Amortization of goodwill | 883 | 883 |
| Interest on long term debt | 26,266 | 25,006 |
| Other interest | <u>26,141</u> | <u>37,760</u> |
| | <u>114,968</u> | <u>113,855</u> |
| | 403,586 | 438,187 |
| SHARE OF EARNINGS (LOSSES) OF COMPANIES ON EQUITY BASIS | <u>(29,040)</u> | <u>41,068</u> |
| CONSOLIDATED INCOME BEFORE INCOME TAXES | 374,546 | 479,255 |
| Income taxes | <u>93,585</u> | <u>105,519</u> |
| CONSOLIDATED INCOME | 280,961 | 373,736 |
| MINORITY INTEREST | <u>98,966</u> | <u>100,363</u> |
| CONSOLIDATED NET INCOME FOR THE YEAR | 181,995 | 273,373 |
| Retained earnings, beginning of year | <u>931,117</u> | <u>692,764</u> |
| | 1,113,112 | 966,137 |
| Dividends | <u>36,007</u> | <u>35,020</u> |
| RETAINED EARNINGS, END OF YEAR | <u>\$1,077,105</u> | <u>\$ 931,117</u> |
| BASIC EARNINGS PER SHARE | <u>\$ 0.25</u> | <u>\$ 0.39</u> |

INDEPENDENT FACTORS LTD.

CONSOLIDATED BALANCE SHEET
AS AT 31 DECEMBER 1986

| | 1986 | 1985 |
|---|--------------------|--------------------|
| ASSETS | | |
| CURRENT | | |
| Cash | \$ 189,554 | \$ 93,704 |
| Marketable securities | 5,606 | 5,227 |
| Accounts receivable | 732,746 | 989,834 |
| Inventories | 1,734,270 | 1,806,483 |
| Prepaid expenses | <u>10,661</u> | <u>14,044</u> |
| | 2,672,837 | 2,909,292 |
| LONG TERM INVESTMENTS, note 2 | 220,394 | 224,021 |
| FIXED, note 3 | 600,519 | 608,415 |
| GOODWILL, note 4 | <u>22,968</u> | <u>23,851</u> |
| | <u>\$3,516,718</u> | <u>\$3,765,579</u> |
| LIABILITIES | | |
| CURRENT | | |
| Bank indebtedness, note 5 | \$ 21,318 | \$ 332,041 |
| Accounts payable | 468,146 | 574,915 |
| Income taxes | 46,255 | 76,008 |
| Current portion of long term debt | <u>80,356</u> | <u>85,595</u> |
| | 616,075 | 1,068,559 |
| LONG TERM DEBT, note 6 | <u>155,660</u> | <u>225,955</u> |
| | 771,735 | 1,294,514 |
| MINORITY INTEREST | <u>391,628</u> | <u>303,262</u> |
| | <u>1,163,363</u> | <u>1,597,776</u> |
| SHAREHOLDERS' EQUITY | | |
| SHARE CAPITAL, note 7 | 1,232,225 | 1,192,661 |
| CONTRIBUTED SURPLUS | 44,025 | 44,025 |
| RETAINED EARNINGS | <u>1,077,105</u> | <u>931,117</u> |
| | <u>2,353,355</u> | <u>2,167,803</u> |
| | <u>\$3,516,718</u> | <u>\$3,765,579</u> |
| SIGNIFICANT ACCOUNTING POLICIES, note 1 | | |
| CONTINGENT LIABILITIES, note 8 | | |
| DIRECTORS REMUNERATION, note 9 | | |

Approved on behalf of the Board:

Lorraine Ben, Director*St. Kast*, Director

INDEPENDENT FACTORS LTD.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
FOR THE YEAR ENDED 31 DECEMBER 1986

| | <u>1986</u> | <u>1985</u> |
|--|-------------------------|---------------------------|
| OPERATING ACTIVITIES | | |
| Operations | | |
| Net income for the year | \$181,995 | \$ 273,373 |
| Items not involving cash | | |
| Amortization of goodwill | 883 | 883 |
| Depreciation | 61,678 | 50,206 |
| Minority interest | 98,966 | 100,363 |
| Cash provided by operations | <u>343,522</u> | <u>424,825</u> |
| Changes in non-cash working capital balances | | |
| Marketable securities | (379) | 12,946 |
| Accounts receivable | 257,088 | (288,342) |
| Inventories | 72,213 | (361,680) |
| Prepaid expenses | 3,383 | (3,084) |
| Accounts payable | (106,769) | 21,686 |
| Income taxes | (29,753) | 23,149 |
| Current portion of long term debt | (5,239) | 36,531 |
| Cash provided by operating activities | <u>534,066</u> | <u>(133,969)</u> |
| FINANCING ACTIVITIES | | |
| Issue of common shares | 39,564 | 147,560 |
| Purchase of common shares | - | (27,893) |
| Increase (decrease) in long term debt | (70,295) | 97,565 |
| Dividends | (36,007) | (35,020) |
| Increase (decrease) in minority interest | (10,600) | 300 |
| | <u>(77,338)</u> | <u>182,512</u> |
| INVESTING ACTIVITIES | | |
| Decrease (increase) in long term investments | 3,627 | (7,626) |
| Purchase of fixed assets | <u>(53,782)</u> | <u>(178,413)</u> |
| | <u>(50,155)</u> | <u>(186,039)</u> |
| INCREASE (DECREASE) IN CASH AND EQUIVALENTS | 406,573 | (137,496) |
| Cash and equivalents, beginning of year | <u>(238,337)</u> | <u>(100,841)</u> |
| CASH AND EQUIVALENTS, END OF YEAR | <u>\$168,236</u> | <u>\$(238,337)</u> |
| Represented by: | | |
| Cash | \$189,554 | \$ 93,704 |
| Bank indebtedness | <u>21,318</u> | <u>332,041</u> |
| | <u>\$168,236</u> | <u>\$(238,337)</u> |

INDEPENDENT FACTORS LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
31 DECEMBER 1986

1. SIGNIFICANT ACCOUNTING POLICIES

The following is a summary of significant accounting policies of the Company:

(a) Principles of Consolidation

The consolidated financial statements include the accounts of the Company and all its subsidiary companies. Acquisitions are consolidated from the date of acquisition applying the purchase method. All significant intercompany transactions and accounts have been eliminated.

(b) Marketable Securities

Marketable securities are stated at cost. Their market value at 31 December 1986 was \$5,679 (1985 - \$7,003).

(c) Inventories

Inventories are stated at the lower of cost and net realizable value with cost being determined on the first-in, first-out basis.

(d) Long Term Investments

Investments in companies in which the Company has significant influence are accounted for by the equity method, by which the original cost of the shares is adjusted for the Company's share of earnings or losses since significant influence was acquired.

(e) Fixed Assets

Fixed assets are stated at cost and depreciation is provided using the diminishing balance method at the following rates:

| | |
|----------------------|-------------|
| Buildings | - 5 and 10% |
| Equipment | - 20% |
| Computer equipment | - 30% |
| Automotive equipment | - 30% |

(f) Goodwill

The amount by which the purchase price of one of the subsidiary companies exceeds the net identifiable assets acquired is treated as goodwill and is amortized over its estimated useful life of thirty years using the straight line method.

2. LONG TERM INVESTMENTS

| | 1986 | 1985 |
|---|-------------------|-------------------|
| Shares in related companies | \$ 760 | \$ 760 |
| Share of earnings in companies accounted for using the equity basis | 19,744 | 48,784 |
| Loans to related companies | 143,970 | 139,609 |
| Other loans | 55,920 | 34,868 |
| | <u>\$ 220,394</u> | <u>\$ 224,021</u> |

3. FIXED ASSETS

| | 1986 | 1985 |
|------------------------------------|-------------------------------------|-------------------------------------|
| | Accumulated Cost Depreciation | Accumulated Cost Depreciation |
| Land | | |
| Buildings | \$ 102,825 | \$ 102,815 |
| Equipment | 548,874 | 548,874 |
| Computer equipment | 224,264 | 132,889 |
| Automotive equipment | 26,280 | 21,863 |
| | <u>128,735</u> | <u>71,973</u> |
| | <u>1,930,968</u> | <u>430,449</u> |
| Cost less accumulated depreciation | <u>\$608,519</u> | <u>977,186</u> |
| | <u>368,771</u> | |

| | 1986 | 1985 |
|----------------------|---------------------------------------|---------------------------------------|
| | Cost Less accumulated amortization | Cost Less accumulated amortization |
| Buildings | \$ 26,500 | \$ 26,500 |
| Equipment | 3,532 | 2,649 |
| Computer equipment | | |
| Automotive equipment | | |
| | <u>\$ 22,968</u> | <u>\$ 23,851</u> |

5. BANK INDEBTEDNESS

| | 1986 | 1985 |
|------------|------------------|------------------|
| Bank loans | \$ 20,000 | \$ 202,159 |
| Overdraft | 1,318 | 29,882 |
| | <u>\$ 21,318</u> | <u>\$332,041</u> |

The bank loans are secured by a general assignment of book debts, inventories and proceeds of certain fire and life insurance policies owned by the Company and its subsidiaries.

INDEPENDENT FACTORS LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
31 DECEMBER 1986

INDEPENDENT FACTORS LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
31 DECEMBER 1986

| 6. LONG TERM DEBT | 1986 | 1985 |
|--|------------------|------------------|
| Bank loans, repayable in monthly instalments, of \$5,850 plus interest at prime plus 1%, secured by a demand debenture and collateral mortgage on land and buildings | \$216,992 | \$289,452 |
| Due to shareholder, repayable at \$1,000 monthly including interest at prime plus 2% | 19,024 | 22,098 |
| Current portion | 236,016 | 311,550 |
| | 80,356 | 85,595 |
| | <u>\$155,660</u> | <u>\$225,955</u> |

Principal payments due in the next four years are as follows:

| | | |
|------|---|-----------|
| 1987 | — | \$ 80,356 |
| 1988 | — | 79,632 |
| 1989 | — | 67,465 |
| 1990 | — | 8,562 |

\$236,016

| 7. SHARE CAPITAL | 1986 | 1985 |
|------------------|---|--------------------|
| Authorized | | |
| 3,000,000 | Class "A" common, voting shares of no par value | |
| 5,000,000 | Class "B" common, non-voting shares of no par value | |
| 400,000 | 8% non-cumulative, redeemable preferred shares of par value of \$5 each | |
| Issued | | |
| 720,144 | Class "A" common, voting shares (1985 - 707,304 shares) | \$1,232,225 |
| | | <u>\$1,192,661</u> |

During the year 12,840 (1985 - 56,502) common shares were issued for a cash consideration of \$39,564 (1985 - \$147,560). During the prior year 42,912 common shares were repurchased for a cash consideration of \$27,893.